



SECTION 9

Guidelines for Expected Use of Bond and COP Proceeds

9.1 Background

These guidelines should be used in preparing capital budget requests for projects funded by bonds and certificates of participation (COP). They apply to all projects identified in CBS with proposed appropriations and/or reappropriations of more than or equal to \$250,000 from the following list of funds or any COP funded projects:

- 01L Higher Education Construction Account
- 045 State Vehicle Parking Acct
- 051 State & Local Improv. Rev. Acct (Waste Disp. Fac.)
- 055 State & Local Improv. Rev. Acct (Waste Disp. 1980)
- 057 State Building Construction Account
- 070 Outdoor Recreation Account
- 072 State & Local Improv. Rev. (Water Supply Fac.)
- 244 Habitat Conservation Account
- 350 Capitol Historic District Acct
- 355 State Taxable Building Construction Account
- 357 Gardner-Evans Higher Education Construction Account

IRS limits on tax-exempt bonds

The Internal Revenue Code limits the amount of proceeds of any issue of tax-exempt bonds that may be used to finance activities or facilities used for nongovernmental purposes. In general, no more than the *lesser* of 10 percent or \$15 million of proceeds of any tax-exempt bond issue may be used for any nongovernmental use, of which no more than the *lesser* of 5 percent or \$5 million may be used to make any loans to nongovernmental persons.

This guideline helps determine if a project is for governmental or nongovernmental purposes, and, as such, helps determine whether an appropriation should be made from tax-exempt bond/COP proceeds or from taxable bond/COP proceeds.

Please prepare a separate “Expected Use of Bond/COP Proceeds” form for each proposed project with appropriations and/or reappropriations of \$250,000 or more and maintain it on file. (Form is available in Appendix D.)

If the determination is that the project qualifies for nontaxable funding then request funding from your usual and accustomed funding source. If the determination is that the project requires taxable funding, request funding from Fund 355 (State Taxable Building Construction Account).

Definitions of purposes

In preparing the “Expected Use of Bond/COP Proceeds” form, please consider the definitions for *nongovernmental purposes* and *governmental purposes* contained in the glossary, as well as the examples below.

Keep federal tax rules in mind

In determining whether bond/COP proceeds are considered to be used for governmental or nongovernmental purposes, the following federal tax rules should be kept in mind:

- You must take into account reasonably expected direct and indirect uses of both the proceeds and the financed property during the entire term of the bonds/COPs that will finance that property.
- Nongovernmental use may occur as the result of ownership of the financed property by a nongovernmental person or use of the financed property by a nongovernmental person under a lease, management contract, output contract, or any other arrangement that provides special legal entitlements to the nongovernmental person for beneficial use of the bond-financed property.
- Generally, the ultimate use of the financed property determines the character of the use of the financed property.

Overall, all of the facts and circumstances concerning arrangements with nongovernmental entities for use of the bond/COP-financed property must be considered.

Examples

1. If proceeds are loaned to a housing authority to build an apartment building that the housing authority leases to a separate partnership in which the housing authority is the general partner and private investors are limited partners, the financed apartment building is considered used for nongovernmental purposes.
2. If proceeds are loaned to a city to build a sewage treatment plant, but the city enters into a long-term management contract with a private company to operate the sewage treatment plant for the city, and the management contract fails to meet Internal Revenue Service requirements for a "qualified management contract," the treatment plant is considered used for a nongovernmental purposes.
3. If proceeds are loaned to a port district to build a dock that the port district leases long-term to a private shipping company, the dock is considered used for nongovernmental purposes.

4. If a state agency leases excess office space in a bond or COP-financed building to commercial businesses, the portion of the proceeds properly allocated to the cost of that space is considered used for nongovernmental purposes.
5. If the estimated useful life of a project is shorter than the term of the financing and the project will be sold or leased to a private nonprofit corporation before the end of the financing, the project is considered used for nongovernmental purposes.